Business Series
IR2003

Inland Revenue

Supplying services. How to calculate the deemed payment

We produce a wide range of leaflets, booklets and Helpsheets designed to explain different aspects of the tax and National Insurance systems in plain English and to assist in the completion of tax returns. Most of them are free. Some you might find particularly helpful are listed below.

IR56 Employed or self-employed? A guide for tax and National Insurance
IR109 Employer compliance reviews and negotiations
IR125 Using your own car or motorbike for work
IR175 Supplying services through a limited company or partnership

CWG2 Employer's further guide to Pay As You Earn and National Insurance contributions

480 Expenses and benefits. A tax guide
490 Employee travel. A tax and NICs guide for employers

IR206 Helpsheet: Capital allowances for employees and office holders

Our leaflet IR120 'You and the Inland Revenue' tells you more about the standard of service you can expect and the steps to take if you want to comment on the service you receive, or complain about the way we have handled your tax and National Insurance affairs.

Our IR List 'Catalogue of leaflets and booklets' gives further information about our publications, most of which you can get from any Inland Revenue Enquiry Centre, Tax Office or Inland Revenue National Insurance Contributions Office. Addresses are in your local phone book under 'Inland Revenue'. Most offices are open to the public from 8.30am to 4.30pm, Monday to Friday and some are also open outside these hours.

Your local library or Citizens' Advice Bureau may also have copies of our leaflets.

You can also get most of our leaflets by

- calling our Orderline on **0845 9000 404** between 8.00am and 10.00pm, seven days a week (except Christmas Day). Orderline calls are charged at local rates
- fax on **0845 9000 604**
- e-mail on **saorderline.ir@gtnet.gov.uk**

Many leaflets are also available on the Internet at **www.inlandrevenue.gov.uk**

Tax Bulletin
This is produced six times a year and shows some of our current thinking on technical aspects of taxation. The bulletin is available on the Inland Revenue website. Paper copies are also available. For further information contact

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London WC2B 6NR

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Do you use a limited company or a partnership to provide your services to clients? If so, you need to know about tax and National Insurance Contributions (NICs) rules which apply from 6 April 2000.

Our leaflet IR175 'Supplying services through a limited company or partnership' tells you what these rules are and explains

- how to decide whether the rules apply to you, and
- what to do if they do apply.

It also answers some common questions and tells you where to get further advice if you are still unclear on any point. Detailed information about all aspects of these rules is available on our website at **www.inlandrevenue.gov.uk/ir35**

If the rules do apply to you, your company or partnership may be treated as making a payment to you (known as the 'deemed payment') which is chargeable to Pay As You Earn (PAYE) tax and NICs.

This leaflet explains

- how to work out the deemed payment, and
- how to pay us the tax and NICs due on any deemed payment.

It also provides answers to some commonly asked questions.

There is an example at the end of the leaflet and a blank step by step guide which you can use for your own calculation.

How to calculate the deemed payment

Your company or partnership should operate PAYE and pay NICs in the usual way on any salary paid to you during the year, and report any taxable benefits (such as a company car) to us on form P11D.

Your company or partnership will also need to work out what the deemed payment is to find out if any additional tax and NICs will be due at the end of the tax year (or earlier in some circumstances, see 'Common Questions' in leaflet IR175).

To work out the deemed payment

1. Add up all the amounts your company or partnership received for your services in the tax year under contracts to which the rules apply (see leaflet IR175 for more details about how to identify such contracts). These amounts may be cash payments or non-cash benefits received by your company or partnership.

   Non-cash benefits might include things like the provision of living accommodation, the use of an asset such as a car, gifts of assets and other benefits or facilities provided by the client. Further guidance about benefits can be found in booklet 480 'Expenses and Benefits. A tax guide'.

   Deduct 5 per cent from this total of salary and benefits. This is to allow for the costs involved in running your company or partnership. This deduction is given automatically, but only affects the calculation of the deemed payment. You cannot deduct it when you are working out the taxable profits of your company or partnership.

2. Add any other payments and the value of any non-cash benefits you have received in the year directly from your client(s) (or from any other third party) and not through your company or partnership, in return for services provided under contracts to which the rules apply, unless PAYE tax has already been deducted from the payments before you get them, or the benefits have been reported to us on form P11D. The benefits referred to here would include the same types of benefits referred to at Step 1 above, such as a car or living accommodation.

3. Deduct certain expenses met by your company or partnership in the year. These are expenses for which you would have been able to have claimed tax relief personally

   - if you had been an employee of your client(s), and

- you had met the expenses yourself out of your salary from your employment.

Employees are only allowed to deduct expenses which are wholly, exclusively and necessarily incurred in the performance of their duties. These will not include some common items, which are deductible in working out the taxable profits of your company or partnership.

For example, where the company or partnership employs a spouse to carry out administrative work for the company, it is unlikely that his or her wages will be allowed when working out the deemed payment. This is because an employee would not have been allowed to deduct those wages when working out his or her taxable earnings from employment.

You may, however, be able to claim for

- travel and related meal and accommodation costs incurred in doing your job or in travelling to a temporary workplace you had to attend to perform your job (see 'Common Questions' in leaflet IR175), and

- other necessary expenses incurred solely in doing your job.

Further guidance about what expenses may be claimed can be found in booklets 480 ‘Expenses and Benefits. A tax guide’ and 490 ‘Employee Travel. A tax and NICs guide for employees’ and in the notes on the Employment Pages of your tax return.

The deductions allowed at this stage in the calculation of the deemed payment do not affect the expenses that can be deducted when working out the taxable profits of your company or partnership.

4. Deduct capital allowances for any equipment or machinery bought by your company or partnership to the extent that you would have been able to claim capital allowances personally

- if you had been an employee of your client(s), and

- had bought the equipment or machinery yourself.

Capital allowances are an allowance for the depreciation of equipment or machinery that it is 'necessary' for you to provide to carry out your duties as an employee. Equipment or machinery is regarded as necessary if you could not do your job without it. The equipment and machinery must be things that every person doing your job would have to provide.

For example, your company or partnership may own computer equipment. However, if your client provides all of the equipment necessary to complete the job and your company or partnership only uses its own equipment out of choice then, in calculating the deemed payment, capital allowances will not be allowed for your company or partnership's equipment.

The 'necessary' test does not apply for cars and bicycles. Therefore, you may be able to claim capital allowances for a car or bicycle that you used for your work or in travelling to a temporary workplace you had to attend to perform your job. Further guidance about claiming capital allowances can be found in leaflet IR125 'Using your own car or motor bike for work' and in Helpsheet IR206: Capital allowances for employees and office holders.

5. Deduct any payments made by your company for your own personal benefit to an approved pension scheme.

6. Deduct any employer's NICs that your company or partnership has already paid on salary paid to you in the year, and Class 1A NICs that will be payable when your form P11D is submitted. The NICs should be calculated on an annual basis, whether or not you are a director of your company (see CWG1 'Employer's Quick Guide to Pay As You Earn and National Insurance contributions', Card 12 Company Directors - National Insurance contributions).

7. Deduct any salary or wages, any payments to reimburse allowable expenses and the value of any benefits in kind you have received from your company or partnership in the year, on which PAYE and NICs have already been paid or will be paid when you send in form P11D.

If the amount you are left with at this point is zero or a negative number there is no deemed payment. However, if the amount you are left with is a positive number, you have to work out the amount which, together with the employer's NICs due on it, comes to the balance calculated after Step 7. The step by step guide at the end of this leaflet shows you how to do this. The result of this calculation is the deemed payment. If the deemed payment is greater than zero you will need to pay some additional tax and NICs.

There is a full example of a calculation of a deemed payment at the end of leaflet IR175. There is also a step by step example guide at the end of this leaflet, as well as a blank guide which you can copy and use for your own calculations.

How to account for the deemed payment

Employer forms

The deemed payment and any tax and NICs due on it should be entered in the normal way on the deductions working sheet. The 'Employers further guide to PAYE and National Insurance contributions' (CWG2) explains how to work out PAYE and NICs for various pay intervals.

Any tax and NICs due at the end of the tax year as a result of the calculation of the deemed payment should be sent to us by 19 April following the end of the tax year in which the deemed payment arises, along with any other tax and NICs due to be paid at that date.

The deemed payment and the tax and NICs due on it should be included in the totals of pay, tax and NICs in the end of year PAYE returns (forms P35 and P14) which you need to send to us by 19 May. The deemed payment should also be included on form P60 which your company needs to give to employees by 31 May.

The deemed payment and any tax and NICs due on it do not have to be identified separately from any other pay, tax and NICs included in your end of year forms. On the P35, the tax and the NICs can simply be included in the total tax and total NICs boxes, but there is a question to answer at box 6 of the checklist on the front of form P35 to tell us whether or not PAYE and NICs on a deemed payment are included in the total figures.

If you are unable to complete your deemed payment calculation by 19 April, we will accept a payment on account at that date of the tax and NICs due on the deemed payment. However, you will need to tell us in a note accompanying your form P35 by 19 May that the amount paid on 19 April and reflected in the end of year forms sent in by 19 May is provisional.

Interest will be due in the normal way on any of the tax or NICs due on the deemed payment that is not paid to us by 19 April, but, as long as you tell us by 19 May that your figures are provisional, no penalties will be charged, provided you send us supplementary forms P35 and P14 and pay any balance of tax and NICs due in respect of the deemed payment by the following 31 January. This concession on penalties will apply for the tax year 2000/01 and will be reviewed to establish whether it should continue to apply for subsequent years.

Self Assessment returns

The deemed payment is treated as income from employment with your company or partnership and the tax is treated in exactly the same way as other PAYE tax.

The pay and tax details should therefore be recorded on your Self Assessment (SA) return on the supplementary employment page relating to your work through your company or partnership. However, as the pay and tax details on the P60 given to you by your company or partnership should include the deemed payment and the tax, there is no need to enter the figures separately on the employment page. You simply enter the total P60 pay and tax figures in the relevant boxes. If, however, only a provisional amount of tax has been paid by the time you get your P60, you may receive a revised one when the correct deemed payment is calculated and tax accounted for. In such a case, you should use the pay and tax figures on the revised P60.

Company or partnership accounts

Your company or partnership may deduct the deemed payment and any employer's NICs due on it in calculating its tax liability, whether or not the amount is actually paid in the form of salary. This deduction is only allowable in calculating the taxable profits for the accounting period in which the deemed payment is treated as paid. It does not affect your company's or partnership's tax computations for other purposes, which should only show the salary it has actually paid.

Common Questions

What happens to the deemed payment at the end of the tax year?

The deemed payment is simply a means of calculating any tax and NICs due. Your company does not have to pay anything to you, but it does have to pay the tax and NICs to us.

What if the money is paid to me as a salary after the end of the tax year, rather than as dividends?

Any money paid as salary will be subject to the normal PAYE and NICs rules, whenever that salary is paid. Any salary paid in a later year will reduce the amount of the deemed payment in the tax year in which it is paid.

If your company pays you a salary after the end of a tax year in which you have paid tax and NICs on a deemed payment, and your salary in the later year is more than the amount your company receives from engagements covered by the legislation, after deductions, then you may pay more tax and NICs than you need. You should seek advice from your professional adviser if you think this situation applies to you.

What happens if my company does not pay me any salary?

If your company is treated as making a deemed payment to you, but actually uses the money to pay dividends to you (or others), then the rules ensure that those dividends can be paid without further tax becoming due. The dividends can be paid during the same tax year as the deemed payment or in a subsequent year.

Your company should write and tell us about any dividends it has paid which it wants to be exempted under this rule. We will need the following information.

- The name and tax reference of the company making the claim.
- The name(s) and tax reference(s) of the person(s) who received the dividend(s).
- The amount of the dividend paid to each person and the total amount paid.
- The date (or dates) the dividend was paid.
- The amount of the deemed payment and the date on which it was treated as paid.

The person who has received the dividend does not have to do anything to claim any relief.

What happens if my company or partnership fails to follow these rules?

If your company or partnership fails to follow these rules and does not pay the tax and NICs due, we will seek to collect any unpaid tax or NICs and any interest due. In addition, penalties may be sought in cases of negligent or fraudulent conduct. Details of the relevant procedures are set out in leaflet IR 109 'Employer compliance reviews and negotiations'.

What key dates do I need to remember?

5th April	-	Calculate your deemed payment.
19th April	-	Send us any tax and NICs due on the deemed payment, or a payment on account of any tax and NICs due.
19th May	-	Send your End of Year PAYE returns (forms P35 and P14) to us and include any deemed payment and tax and NICs due in it on these forms; if you have not yet finally calculated your deemed payment, then tell us in a covering letter that your figures are only provisional.
31st January	-	If you only sent us provisional figures on 19 May, then send us corrected form P35 and P14 figures now, and pay any balance of tax and NICs due at the same time. If necessary, issue a corrected P60 to your employee at the same time. If you do not do this, penalties may apply.

Where can I find more help?

We have published a lot of material about the service provision legislation on a dedicated Inland Revenue website at **www.inlandrevenue.gov.uk/ir35**. This includes answers to frequently asked questions.

If you do not have access to the website, you can phone the 'IR35' Helpline on **0845 303 3535** and they will send you paper copies of all the material on the website, including the frequently asked questions.

What if I need advice about a particular contract?

You can ask us to give opinions on whether the new rules apply to a particular engagement. Our opinion will be based on the existing case law tests for deciding employment status. We will be bound by our opinion, as long as you have given us the full facts.

If you want us to give an opinion, you should send us copies of any contracts involved in the engagement, together with any other information that you think might be relevant. Sometimes we may have to ask you for further information about the engagement and may also need to speak to your client(s) so that we can establish the full facts.

If you would like our opinion on a particular engagement you should send your contract(s) to:

IR35
Penhaligon House
Trinity Street
St Austell
Cornwall
PL25 5BA

Fax. **0845 302 3538**

Calculation of the Deemed Payment

Example using the step by step guide

(Using 2000/01 rates, thresholds and allowances.)

Mrs Worker works through her own limited company. She provides services to Mrs Client under a contract which falls within the new rules. Mrs Client pays £40,000 to Mrs Worker's limited company for the services provided by Mrs Worker.

Mrs Worker does no other work in the year in question. She pays herself a salary of £10,000 during the course of the year and operates PAYE and deducts NICs from that salary in the usual way. She also has a company car available for her private use which is treated as a taxable benefit in kind valued at £2,000.

Mrs Worker's company meets the car's running costs of £3,000. The car is used 50% for business travel and 50% for private purposes. The amount which Mrs Worker could have claimed as a Schedule E deduction if she had worked directly for Mrs Client and had paid them herself is £1,500. Similarly, capital allowances would have been £1,500.

Mrs Worker's company also pays £2,000 into her personal pension scheme.

Step One	Enter in this box the amount of all payments and benefits received by your company or partnership in the year for contracts to which these rules apply.	1	£40,000
	Enter in this box 5% of the amount in box 1.	2	£2,000
Step Two	Enter in this box the amount of any payments and benefits received directly by you in the year for contracts to which the rules apply and which are not already taxable.	3	0
Step Three	Enter in this box the amount of any expenses met by your company or partnership in the year which you could have claimed personally if the worker had been an employee of the client and had paid for them yourself.	4	£1,500
Step Four	Enter in this box the amount of any capital allowances for purchases made by your company or partnership which you could have claimed yourself if you had been employed by your client and had made the purchases yourself.	5	£1,500

Step Five	Enter in this box the amount of any contributions to an approved pension scheme made by your company or partnership for your personal benefit.	6	£2,000
Step Six	Enter in this box the amount of any employer's Class 1 and Class 1A NICs which your company or partnership paid for the year in respect of salary or non-cash benefits which it provided to you in the year.	7	£929
Step Seven	Enter in this box the amount of any salary and the value of any non-cash benefits you received from your company or partnership in the year which are already taxable (this does not include anything for which a deduction has already been given at Step Three).	8	£12,000
	Add together the figures in boxes 1 and 3 and enter the total in this box.	9	£40,000
	Add together the figures in boxes 2, 4, 5, 6, 7, and 8 and enter the total in this box	10	£19,929
	Deduct the figures in box 10 from the figures in box 9 and enter the answer in this box. If the answer in box 11 is nil or a negative number there is no deemed payment. If the answer in box 11 is a positive number you will need to process this figure to get the deemed payment and the employer's Class 1 NICs on that deemed payment.	11	£20,071
	Multiply the figure in box 11 by 100 and enter the answer in this box.	12	£2,007,100
	Divide the figure in box 12 by (100+12.2) (see footnote)[1] and enter the answer in this box. The figure in box 13 is the deemed payment.	13	£17,888

Step Seven	Deduct the figure in box 13 from the figure in box 11 and enter the amount you are left with in this box. This amount is the amount of employer's Class 1 NICs due on the deemed payment.	14	£2,183

[1] The employer's contribution rate can vary. Contracted-out or in-rates are different. The figure you add to 100 at this stage should be the contributions rate that is applicable to you. See Inland Revenue National Insurance tables CA38 and the Employer's Annual Pack for further details.

Calculation of the Deemed Payment Step by step guide

Step One	Enter in this box the amount of all payments and benefits received by your company or partnership in the year for contracts to which these rules apply	1	
	Enter in this box 5% of the amount in box 1	2	
Step Two	Enter in this box the amount of any payments and benefits received directly by you in the year for contracts to which the rules apply and which are not already taxable.	3	
Step Three	Enter in this box the amount of any expenses met by your company or partnership in the year which you could have claimed personally if the worker had been an employee of the client and had paid for them yourself.	4	
Step Four	Enter in this box the amount of any capital allowances for purchases made by your company or partnership which you could have claimed yourself if you had been employed by your client and had made the purchases yourself.	5	
Step Five	Enter in this box the amount of any contributions to an approved pension scheme made by your company or partnership for your personal benefit.	6	
Step Six	Enter in this box the amount of any employer's Class 1 and Class 1A NICs which your company or partnership paid in the year in respect of salary or non-cash benefits which it provided to you in the year.	7	
Step Seven	Enter in this box the amount of any salary and non-cash benefits you received from your company or partnership in the year which are already taxable (this does not include anything for which a deduction has already been given at Step Three).	8	

Step Seven	Add together the figures in boxes 1 and 3 and enter the total in this box.	9	
	Add together the figures in boxes 2, 4, 5, 6, 7, and 8 and enter the total in this box	10	
	Deduct the figures in box 10 from the figures in box 9 and enter the answer in this box. If the answer in box 11 is nil or a negative number there is no deemed payment. If the answer in box 11 is a positive number you will need to process this figure to get the deemed payment and the employer's Class 1 NICs on that deemed payment.	11	
	Multiply the figure in box 11 by 100 and enter the answer in this box.	12	
	Divide the figure in box 12 by (100+12.2) (see footnote)[2] and enter the answer in this box. The figure in box 13 is the deemed payment.	13	
	Deduct the figure in box 13 from the figure in box 11 and enter the amount you are left with in this box. This amount is the amount of employer's Class 1 NICs due on the deemed payment.	14	

[2] The employer's contribution rate can vary. Contracted-out or in-rates are different. The figure you add to 100 at this stage should be the contributions rate that is applicable to you. See Inland Revenue National Insurance tables CA38 and the Employer's Annual Pack for further details.

Our service commitment to you

The Inland Revenue and Customs & Excise are committed to serving your needs well by

acting fairly and impartially

We

- treat your affairs in strict confidence, within the law
- want you to pay or receive only the right amount due.

communicating effectively with you

We aim to provide

- clear and simple forms and guidance
- accurate and complete information in a helpful and appropriate way.

providing good quality service

We aim to

- handle your affairs promptly and accurately
- be accessible in ways that are convenient to you
- keep your costs to the minimum necessary
- take reasonable steps to meet special needs
- be courteous and professional.

taking responsibility for our service

- We publish annually our customer service aims and achievements.
- If you wish to comment, or make a complaint, we want to hear from you so we can improve our service. We advise you how to do this.

We can provide better service if you help us by

- keeping accurate and up to date records
- letting us know if your personal/business circumstances change
- giving us correct and complete information when we ask for it
- paying on time what you should pay.

Further information on customer service is available at Inland Revenue and Customs and Excise local offices, set out in our Charters, complaints leaflets (IR120 and Notice 1000) and Codes of Practice.

These notes are for guidance only and reflect the tax and NICs position at the time of writing. They do not affect any right of appeal.

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